No. 10759

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

CHIQUITA MINING COMPANY, LTD.,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

BRIEF OF PETITIONER.

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Statement of Pleadings and Facts Relative to Jurisdiction.

1. On May 1, 1941, a notice of deficiency [Tr. of Rec., pp. 11 to 21, incl.] was mailed to petitioner.
2. The taxes in controversy were income and excess profits taxes for the calendar years 1936, 1937, 1938, and 1939, in the total amount of $11,861.65.
3. On July 29, 1941, petitioner's original petition for redetermination (not included in the record here) was filed.
4. On August 19, 1941, petitioner's amended petition for redetermination [Tr. of Rec., pp. 4 to 21] was filed.
5. On September 25, 1941, an answer [Tr. of Rec., pp. 21 to 23] was filed.

6. On August 26, 1942, pursuant to request previously made by petitioner, the hearing on the issues presented by the amended petition and answer thereto was set for October 12, 1942, at Los Angeles, California.

7. On October 14, 1942, the hearing was commenced, and completed on October 15, 1942. The matter was submitted on briefs to be filed by counsel for both parties.

8. On January 5, 1943, a memorandum opinion was rendered by the Judge who heard the matter.

9. On February 4, 1943, a motion to reopen the cause for the presentation of further evidence was filed by petitioner, together with evidence in support thereof.

10. On February 6, 1943, the motion was denied.

11. On April 8, 1943, decision under Rule 50 was entered.

12. On July 6, 1943, petition for review by the United States Circuit Court of Appeals for the Ninth Circuit with assignments of error was filed by petitioner.

13. The time of petitioner to have prepared and transmitted the record herein to the United States Circuit Court of Appeals for the Ninth Circuit having been extended by orders of said Court to May 1, 1944, said record was duly filed with the Clerk of said Court on said date.

14. The jurisdiction of the Board of Tax Appeals, now the Tax Court of the United States, to enter its decision herein, and the jurisdiction of the United States Circuit Court of Appeals for the Ninth Circuit to review the decision of the Tax Court of the United States, is provided for and governed by the 1926 Revenue Act, approved February 26, 1926, as amended by the various revenue acts enacted and approved prior to the date of the filing of petitioner's petition for review herein.

Statement of Case.

In its amended petition for redetermination, petitioner contended that the determination of the tax set forth in respondent's notice of deficiency was based upon the following errors:

1. That the Commissioner erred in his computation of the cost of mining property upon which depletion is allowable.

2. That the Commissioner erred in his estimate of the usable life of machinery and equipment, upon which depreciation deduction is based.

Since the Tax Court of the United States held that the contention of petitioner on the depreciation question was correct, that issue is not here involved.

On the issue with reference to depletion, the Court held that:

> "No evidence was offered on the first issue and respondent's determination on this point is consequently approved."

On the question of depletion, the ultimate fact to be determined was the cost to petitioner of certain mining properties which were conveyed to it shortly after the organization of the corporation. These properties were conveyed to the corporation by Jack H. Smith and Otto F. Schwartz in consideration of the issuance to them and to a third party of certain shares of the capital stock of petitioner. The primary question to be determined was whether the said Jack H. Smith and Otto F. Schwartz were, after the conveyance by them of these mining properties to petitioner, in as much control of petitioner's affairs as they had been in control of said mining properties prior to the conveyance of said mining properties to petitioner and the issuance of said capital stock in consideration thereof. If Jack H. Smith and Otto F. Schwartz were in as much control of petitioner's affairs after the conveyance of said mining properties and the issuance of said capital stock as they had been in control of said mining properties, then the transactions in connection therewith would not have constituted a taxable transfer, and hence, the cost to petitioner would have been deemed to be the same as the cost to the vendors, Jack H. Smith and Otto F. Schwartz. If, on the contrary, Jack H. Smith and Otto F. Schwartz were not in as much control of petitioner's affairs after the conveyance of said mining properties and the issuance of said capital stock as they had been in control of said mining properties, then the cost to petitioner would not have been deemed to be the same as the cost to the vendors, but evidence would have been admissible to show the true consideration paid by petitioner as the cost of said mining properties. Respondent had computed petitioner's tax liability on the first of these two theories.

The third party to whom we have referred above as the party to whom petitioner issued and delivered certain capital stock, was James Maxfield, doing business in the county of Clark, state of Nevada, where the mining properties were located and petitioner had its principal place of business, under the fictitious firm name and style of CHIQUITA MINE SYNDICATE.

Another most important fact which must be borne in mind is that at the time of the hearing on October 14 and 15, 1942, all agreements, written and verbal, with reference to the conveyance of said mining properties, the issuance and delivery of said capital stock, and in particular the purchase by the Chiquita Mine Syndicate of all shares of such capital stock that had been issued and delivered to Jack H. Smith and Otto F. Schwartz, had been fully executed by all parties and the full consideration for the entire transaction had been paid.

In determining the question concerning whether Jack H. Smith and Otto F. Schwartz were in as much control of petitioner's affairs after the conveyance of the mining properties and the issuance of the capital stock, as they had been in control of said mining properties before the conveyance thereof to petitioner and the issuance by petitioner of its capital stock, the first inquiry should have been the following: What percentage of the issued and outstanding capital stock of petitioner did Jack H. Smith and Otto F. Schwartz own when they conveyed the mining properties to petitioner and petitioner issued and delivered its capital stock therefor? In other words, since Jack H. Smith and Otto F. Schwartz, as owners of said mining properties, had one hundred per cent control over such mining properties, it is obvious that they would have

to have one hundred per cent, or at least fifty-one per cent or more, control, by their stock ownership, over the affairs of petitioner, in order that it could be held and determined that they were in as much control of the affairs of petitioner after the conveyance of mining properties and issuance of capital stock as they had been in control of said mining properties prior to the conveyance of the properties and the issuance of the stock.

The method of showing the control of Jack H. Smith and Otto F. Schwartz over the affairs of petitioner was and is the elementary method of showing control over the affairs of any corporation. As ordinarily happens, the right to elect a majority of the board of directors of a corporation is determined by the ownership of more than fifty per cent of the issued and outstanding capital stock of such corporation. Petitioner was prepared to show that at no time did Jack H. Smith and Otto F. Schwartz ever own more than fifty per cent of the issued and outstanding capital stock of petitioner.

This proof alone would have been sufficient, in our opinion, to have constrained the Tax Court to find that Jack H. Smith and Otto F. Schwartz were not in as much control of the affairs of petitioner after they had conveyed the mining properties to petitioner and petitioner had issued its capital stock in payment therefor, as they had been prior thereto, in control of said mining properties.

When this matter was called for trial on October 14, 1942, this was the first time that the matter had been brought on for hearing. No previous continuance had ever been granted. After the hearing had commenced, James Maxfield, one of the principals involved in the transaction wherein and whereby petitioner acquired the

mining properties in question and the party to whom petitioner issued one-half of the total number of shares of its capital stock as the consideration for the conveyance to it of said mining properties, was called as a witness by petitioner. He exercised his constitutional privilege to refuse to answer any questions put to him with reference to such transaction on the ground that his testimony might tend to incriminate him in certain criminal proceedings pending against him in the District Court of the United States, in and for the District of Nevada. Petitioner thereupon moved for a continuance of the hearing until such time as the testimony of this witness would be available. The motion for a continuance was denied.

When petitioner sought to prove the details of the transaction relative to the conveyance to petitioner of said mining properties and the issuance by petitioner of its capital stock in payment therefor, the presiding Judge of the Tax Court ruled that this could be done in only one manner, and that is by the introduction of original written agreements that had been executed by the parties to the transaction. When petitioner proceeded to make a showing to account for its inability to produce the original agreements in question, in order to introduce secondary evidence concerning the contents of said agreements, counsel for respondent interrupted and made the following statement:

> ". . . I am willing to listen to any secondary evidence he has to offer. I thought that was the purpose of Your Honor's statement just now, to permit him to offer secondary evidence, and I see no purpose in him making this statement at this time."

To this remark Mr. Steffes, one of counsel for petitioner, made the following reply:

> "Well, the secondary evidence, may I suggest to counsel, for the enlightenment of Your Honor, would be my personal knowledge of those documents which I personally prepared and some of which, at least, I personally turned over to Mr. Crupf of the S. E. C., and by reason of which we had been unable to get the original documents or to locate where they are. The situation is this . . ."

The Court then interrupted and a discussion concerning what petitioner had to prove in these proceedings ensued. In this discussion Mr. Sandrich, a Certified Public Accountant and one of counsel for petitioner, indicated that he desired to offer his entire audit records of petitioner as other evidence of the transaction in question. This offer was rejected, and the hearing brought to a summary close by the Judge who presided without having permitted petitioner to prove the details of the transaction by the secondary evidence of Mr. Steffes, or the secondary evidence of the Certified Public Accountant who had made a complete audit of the affairs of petitioner since its incorporation.

Thus, even though counsel for respondent had in effect stipulated to the introduction of such secondary evidence, petitioner was prevented from sustaining its burden of proof by competent evidence other than the introduction of the original agreements which petitioner was unable to produce in court.

After the memorandum opinion was rendered by the Judge who heard the matter, a motion to reopen the cause for the presentation of further evidence was filed by peti-

tioner, together with evidence in support thereof. This evidence tended to show a sufficient reason and excuse for not having presented the evidence required by the Judge on the question of depletion. No counter showing was made by respondent. The motion was denied.

Thereafter, decision under Rule 50 was entered, and within the time provided by law, petitioner filed this petition for review.

Specification of Errors.

I.

The Court erred in denying petitioner's motion for a continuance, particularly after the refusal of James Maxfield and Hugh Wilton to testify.

II.

The Court erred in holding that evidence was immaterial to the effect that on two prior occasions the Internal Revenue Department had held that the cost to petitioner of the mining properties in question was $500,000.00, and that upon each of said occasions petitioner paid an additional tax based on such determination.

III.

Counsel for the Commissioner having agreed to the introduction of secondary evidence in lieu of certain written documents, the Court erred:

(a) In restricting the proof to such written documents;

(b) In rejecting the secondary evidence of the attorney for petitioner, concerning the consideration for said mining

properties paid by petitioner, and that *portion* of said consideration which was received by the vendors, Jack H. Smith and Otto F. Schartz, upon the question as to whether said vendors were at any time thereafter in as much control of petitioner's affairs as they had been prior to the acquistion of said properties by petitioner;

(c) In rejecting the secondary evidence of Mark J. Sandrich, C. P. A., on the same subject;

(d) In rejecting the books and records of petitioner in the possession of said Mark J. Sandrich, C. P. A., on the same subject.

IV.

The Court erred in rejecting evidence on the question as to whether the Commissioner was estopped to deny the cost to petitioner of said mining claims to be $500,000.00, by reason of two previous determinations to that effect by the Internal Revenue Department.

V.

The Court erred in denying petitioner's motion to reopen this cause for the presentation of further evidence upon the issue of the allowance of a proper rate for depletion of the ores in the properties owned by the petitioner.

* * * * * * * * *

We shall treat each of the errors specified in the order set forth above.

I.

The Court Erred in Denying Petitioner's Motion for a Continuance, Particularly After the Refusal of James Maxfield and Hugh Wilton to Testify.

The Facts.

The principal question to be determined with reference to the depletion matter herein involved was the cost to petitioner of the mining properties in question. The transaction wherein and whereby petitioner acquired said mining properties involved three parties. The first party were the vendors who conveyed the properties to petitioner. The second party was petitioner, which issued five hundred thousand shares of its capital stock as the consideration for the conveyance of said mining properties. The third party was James Maxfield, doing business under the fictitious firm name and style of Chiquita Mine Syndicate, who received one-half of the consideration paid for said mining properties by petitioner.

When Mr. Maxfield was called to the witness stand, he refused to answer questions put to him on the ground that his testimony might tend to incriminate him in certain criminal proceedings pending in the United States District Court, in and for the District of Nevada. [Tr. of Rec., pp. 75 to 80.]

Mr. Hugh Wilton, who was associated with Mr. Maxfield in the financing of petitioner, likewise refused to testify on the same ground. [Tr. of Rec., pp. 81 to 83.]

ARGUMENT.

One of the subordinate questions essentially connected with the question of the nature and extent of the control exercised by Jack H. Smith and Otto F. Schwartz over the affairs of petitioner after it had acquired said mining properties, was whether Jack H. Smith and Otto F. Schwartz had acquired sufficient shares of the capital stock of petitioner to elect a majority of its board of directors. The answer to this question depended upon the proportion of such stock which Jack H. Smith and Otto F. Schwartz received out of the total issued and outstanding shares of the capital stock of petitioner. If the Chiquita Mine Syndicate received one-half of such issued and outstanding shares and later acquired the remaining one-half of said shares, then Jack H. Smith and Otto F. Schwartz never did own a sufficient number of the issued and outstanding shares of the capital stock of petitioner to be able to elect a majority of its board of directors, in order thereby to control its affairs.

Obviously, James Maxfield, as the Chiquita Mine Syndicate, was a competent witness to testify concerning his ownership of shares of the capital stock of petitioner, and the time when and parties from whom he had acquired such shares of petitioner's capital stock. When the presiding Judge denied the motion for a continuance after the refusal of these two witnesses to testify, he thereby prevented petitioner from presenting competent evidence from which the Court could have determined that the

transaction wherein petitioner acquired said mining properties was not a nontaxable transfer. This error on the part of the Court was rendered more prejudicial in view of the Court's subsequent refusal to permit the introduction of secondary evidence in lieu of certain written agreements, and its action in restricting the proof to such written instruments, which petitioner was unable to produce at the hearing.

AUTHORITIES.

Continuances are within the discretion of the trial court.

Woods v. Young, 8 U. S. 237, 4 Cranch. 237, 2 L. Ed. 607;

Thompson v. Selden, 61 U. S. 194, 20 How. 194, 15 L. Ed. 1001;

McFaul v. Ramsey, 61 U. S. 523, 20 How. 523, 15 L. Ed. 1010.

It is only necessary for a party to show due diligence to entitle him to a continuance.

Pennington v. Scott, 2 U. S. 94, 2 Dall. 94, 1 L. Ed. 304.

A party may have a continuance on showing reasonable cause.

Schlosser v. Lesher, 1 U. S. 411, 1 Dall. 411, 1 L. Ed. 200;

Bowen v. Douglass, 2 U. S. 44, 2 Dall. 44, 1 L. Ed. 282.

II.

The Court Erred in Holding That Evidence Was Immaterial to the Effect That on Two Prior Occasions the Internal Revenue Department Had Held That the Cost to Petitioner of the Mining Properies in Question Was $500,000.00, and That Upon Each of Said Occasions Petitioner Paid an Additional Tax Based on Such Determination.

The Facts.

At the hearing, petitioner desired and attempted to show that on two prior occasions the Internal Revenue Department of the United States had determined and held that the cost price to petitioner of the mining properties in question was $500,000.00. This determination of said cost price was made for the purpose of ascertaining the proper amount of tax and penalty which should be paid by petitioner as the result of this precise transaction. In the first instance petitioner had paid the documentary stamp tax (due on the issuance of shares of its capital stock) on only those shares for which certificates had actually been issued and delivered. These amounted to approximately 135,000 or 140,000 shares. In May, 1933, the Collector of Internal Revenue in Nevada contended that in contemplation of law the entire purchase price of 500,000 shares of its capital stock was deemed issued and delivered when the mining properties were conveyed to petitioner, notwithstanding the fact that certificates representing all of said 500,000 shares of stock were not issued at the same time. At that time petitioner paid a deficiency documentary stamp tax on the balance of the 500,000 shares for which certificates had not previously been issued, and also paid a penalty.

In the second instance, the value of these shares which were given as the cost price of the mining properties was definitely fixed by the government at $500,000.00. On this occasion the question arose as to the documentary stamp tax that should be affixed by petitioner to the deeds which conveyed certain of these mining properties to petitioner. At that time, in July, 1934, petitioner paid an additional documentary stamp tax based upon the theory of the Internal Revenue Department that the consideration paid by petitioner for the mining properties was $500,000.00, the par value of the 500,000 shares which were issued by petitioner as the consideration for its acquisition of the mining properties. [Tr. of Rec., pp. 59 to 61.]

Argument.

When we consider that one of the most important questions to be determined in this matter of depletion, was whether the transaction in which petitioner acquired these mining properties was a taxable or non-taxable transaction, the materiality and relevancy of this proffered evidence becomes immediately apparent. When counsel for petitioner indicated that they intended to submit this evidence, the presiding Judge made the statement:

> "I think all that is utterly immaterial."

He later added:

> "We have no information, nor are we the slightest bit concerned with what the Bureau of Internal Revenue has done in the past. We are trying your case just like you are entering into the Federal District Court to try it, and we have none of the records, none of the information; only this determination."

Counsel for petitioner then remarked:

> "Well, we had intended to supply that information in the form of legal evidence." [Tr. of Rec., p. 61.]

As we shall show hereafter, the presiding Judge seemed to feel and indicated that the cost to petitioner of the mining properties in question could be shown in only *one* way, that is, by the introduction into evidence of certain written agreements which had been executed at the time of and subsequently to the acquisition of the mining properties by petitioner.

When the Internal Revenue Department, in the second instance mentioned above, required petitioner to pay a deficiency documentary stamp tax with reference to the stamps to be affixed to the deeds which conveyed the mining properties to petitioner, it directly determined the question whether the transaction was a taxable or non-taxable transaction. It also directly determined the question whether the cost to petitioner of said mining properties was deemed to be the cost of said properties to the original vendors, Jack H. Smith and Otto F. Schwartz.

It must be borne in mind that in the present proceedings, respondent has contended that the transaction in question was a non-taxable transaction and therefore that the consideration paid by petitioner should be deemed to be the same as that which was originally paid by said vendors.

However, on the previous occasion last above mentioned, the Bureau of Internal Revenue held that the consideration paid by petitioner was deemed to be $500,000.00. Consequently, we feel that petitioner had the right to set

up the sum of $500,000.00 as the cost price to it of the mining properties in question for the purpose of establishing a cost depletion rate.

Although we felt that we were entirely justified in setting up the sum of $500,000.00 as the cost price of the mining properties, we were willing to adjust this figure, which represented the par value of 500,000 shares, to the actual consideration in cash which had passed in and as the result of the transaction. We therefore were willing to fix the cost price at $100,000.00. This was equal to the following cash items: the sum of $87,500.00, which was the amount in cash paid by Chiquita Mine Syndicate for the 250,000 shares of petitioner's stock which had originally been issued to Jack H. Smith and Otto F. Schwartz; the sum of $10,000.00 paid by petitioner to one Robbins from whom Jack H. Smith and Otto F. Schwartz had obtained two of the mining properties under a lease with option to purchase; and the sum of $2500.00, which petitioner had paid out in defending and protecting the mining properties from adverse claimants.

As shown in our petition for review [Tr. of Rec., p. 37], the proper assessment should be $1806.55 instead of $7,229.04, as assessed by the Commissioner.

Although respondent will argue that the doctrine of estoppel does not apply to the Internal Revenue Department, we nevertheless contend that the determination of the Internal Revenue Department in the proceedings where the cost price to petitioner was *directly* involved should now be followed where that cost price is only indirectly involved in fixing an income tax to be paid by petitioner. (See authorities cited under Point IV.)

III.

Counsel for the Commissioner Having Agreed to the Introduction of Secondary Evidence in Lieu of Certain Written Documents, the Court Erred:

(A) In Restricting the Proof to Such Written Documents;

(B) In Rejecting the Secondary Evidence of the Attorney for Petitioner, Concerning the Consideration for Said Mining Properties Paid by Petitioner, and That Portion of Said Consideration Which Was Received by the Vendors, Jack H. Smith and Otto F. Schwartz, Upon the Question as to Whether Said Vendors Were at Any Time Thereafter in as Much Control of Petitioner's Affairs as They Had Been Prior to the Acquisition of Said Properties by Petitioner;

(C) In Rejecting the Secondary Evidence of Mark J. Sandrich, C. P. A., on the Same Subject;

(D) In Rejecting the Books and Records of Petitioner in the Possession of Said Mark J. Sandrich, C. P. A., on the Same Subject.

(A) Error in Restricting Proof to Certain Written Documents.

During the hearing, the following colloquy took place among the presiding Judge and counsel for petitioner and respondent:

"Mr. Steffes: I would like to make a showing as the reason for the absence of documentary testimony at this time—well, I would like to make that showing so as to lay the foundation for the production of secondary evidence in lieu of such primary evidence.

The Member: Well, what are you going to do? Go ahead.

Mr. Steffes: In this matter, if the Court please, for a period of approximately 18 months, all of the books and records of the corporation and all of the audit figures, the audit spreads and records of Mr. Sandrich were made (available) to Mr. Crupf of the the S. E. C. I didn't know until about six months after his death—the investigation suddenly stopped and about six months later I found out that he had died. He died about a year ago. By reason of that fact I personally know—

Mr. Tonjes: If Your Honor please, I object to the witness' or counsel's statement as not being material to the proceedings here. I am willing to listen to any secondary evidence he has to offer. I thought that was the purpose of Your Honor's statement just now, to permit him to offer secondary evidence, and I see no purpose in him making this statement at this time.

Mr. Steffes: Well, the secondary evidence, may I suggest to counsel, for the enlightenment of Your Honor, would be my personal knowledge of those documents which I personally prepared and some of which, at least, I personally turned over to Mr. Crupf of the S. E. C., and by reason of which we have been unable to get the original documents or to locate where they are. The situation is this—" [Tr. of Rec., pp. 97 and 98.]

At this point counsel for petitioner was interrupted by the presiding Judge and a discussion then ensued concerning the proof that petitioner was required to make in these proceedings.

The following portion of the statement made by counsel for respondent definitely amounts to an agreement or stipulation that petitioner be permitted to introduce secondary evidence in lieu of the written agreements that were not available:

> "I am willing to listen to any secondary evidence he has to offer. I thought that was the purpose of Your Honor's statement just now to permit him to offer secondary evidence, and I see no purpose in him making this statement at this time." [Tr. of Rec., p. 98.]

Argument.

Despite this agreement to permit secondary evidence, petitioner, as we shall hereinafter show, was prevented from introducing such secondary evidence in the form of testimony of its attorney, testimony of the Certified Public Accountant who made a complete audit of all its books and records, and the books and records of petitioner which had been set up as the permanent records of the corporation.

The error of the presiding Judge relative to our claim that he restricted petitioner to the proof of certain written instruments follows from the consideration of the entire record in this case. In other words, when we realize that every other avenue of proof was closed to petitioner, then it is quite obvious that the presiding Judge unduly and erroneously restricted petitioner in its proof.

AUTHORITIES.

The production of an original document is dispensed with where it cannot be produced because it is destroyed or lost, or cannot be found by search, or is otherwise unavailable.

Wigmore on Evidence (2nd Ed.), & Supp., 1923-1933;

Riggs v. Tayloe, 9 Wheat. 483;

Tayloe v. Riggs, 1 Pet. 591;

Security Tr. Co. v. Robb, 142 Fed. 78;

Corliss v. U. S., 7 Fed. (2d) 455.

(B) Error in Rejecting the Secondary Evidence of the Attorney for Petitioner.

THE FACTS.

In the course of the examination of the attorney for petitioner by Mark J. Sandrich, counsel for petitioner, the questioning was interrupted by the discussion which took place following an objection to a question propounded to the witness by counsel for respondent. That discussion is set forth at length on pages 92 to 95 of the transcript of record.

In this discussion the Court clearly indicated that it would not permit oral testimony as to the transaction which was covered by a written contract unless a showing was first made which would entitle petitioner to use secondary evidence. We refer to the following statement of the Court:

> "I don't see where you are going to produce oral testimony as to a transaction that was covered by a

written contract unless you first make that showing which would entitle you to use secondary evidence." [Tr. of Rec., p. 94.]

Previously, the Court had asked the following question after an objection was made by counsel for respondent to a certain question asked of the attorney for petitioner:

"What are you trying to get, what point, with this witness?"

Counsel for petitioner, who was interrogating the witness, then answered:

"I am trying to establish the fact that this witness knows of his own knowledge certain elements of the agreements and actual occurrences in connection with the transfer of properties to Chiquita Mining Company, Limited, and the issuance of its stock for those properties that result in the owners of the properties not being in control of the corporation after such transfer."

The following discussion then took place:

"The Member: I take it the transaction was in writing. That is, a transaction certainly conveying the mining claims would be.

Mr. Sandrich: Yes, Your Honor.

The Member: And I suppose the agreement to transfer to the corporation for shares of stock was in writing?

Mr. Sandrich: There were a number of agreements. There seemed to have been some confusion in the early stages of the game, Your Honor, and it appears that a number of the matters were handled

in a manner not contemplated or not desired by the parties, and a great number of adjustment, amendments and substitutions were made which result in a very complicated mess, to use that word. Now, Your Honor remarked a while ago that Your Honor was interested in the broad aspects of the thing and was not much concerned with the details but wanted enough to show whether or not this situation resulted in the original owners of the mining claims having the control of the corporation after such transfer.

The Member: But it has got to be in a legal way.

Mr. Sandrich: I am trying to do it in a legal way, Your Honor. I am trying to question this witness.

The Member: The way to do its to first introduce the contracts, put people on the stand to identify them, bring out the minutes of the corporation, if you have anybody who was actually a party to the contract to explain it, bring them and put them on the stand.

Mr. Sandrich: Those are in existence, Your Honor, but they are not in court. Some of those records are in Nevada. Some of those records are in the hands of the Treasury Department, and I believe some of them are in the hands of the S. E. C.

The Member: They all can be reached by a subpoena, anywhere in the United States.

Mr. Sandrich: May we have sufficient time in which to secure those records?

The Member: This is your day in court.

Mr. Sandrich: Well, it seems that if we haven't got the records we haven't got a chance to secure the records, and if Your Honor won't permit our oral testimony . . ." [Tr. of Rec., pp. 92 to 94.]

It was at this point that the Court made the following observation:

> "I don't see where you are going to produce oral testimony as to a transaction that was covered by a written contract unless you first make that showing which would entitle you to use secondary evidence." [Tr. of Rec., p. 94.]

Later on counsel for petitioner did proceed to make a showing which would entitle petitioner to introduce secondary evidence. It was while that showing was being made that counsel for respondent objected to its continuance and indicated acquiescence in the introduction of secondary evidence.

When, however, counsel for petitioner indicated, both to the Court and counsel for respondent, that the secondary evidence sought to be introduced would be his personal knowledge of the documents which he personally prepared, he was interrupted by the Court, and an entirely different subject was injected by the Court into the proceedings at this point.

After both counsel for petitioner had attempted to introduce other secondary evidence, the hearing was summarily closed by the presiding Judge without the petitioner having rested its case. The Court concluded the hearing with the following statement:

> "Well, we will close the record and I will allow the parties thirty days to file a memorandum in support of their position." [Tr. of Rec., p. 106.]

ARGUMENT.

The error in not permitting the secondary evidence of the attorney for petitioner arises from the interruption of the proof which counsel for petitioner indicated he was about to offer, the diverting of the proof to other sources of secondary evidence, and the summary termination of the hearing without permitting petitioner to offer the secondary evidence of its attorney, who had prepared certain of the documents which were not available at the time.

However, in the light of the Court's ruling, which we shall discuss under Point (C) and (D) hereinafter, it is obvious that had a direct ruling been requested of the Court concerning the secondary evidence of the attorney for petitioner, an adverse ruling would have been expressed, as it now must be implied from the proceedings that were had.

AUTHORITIES.

Where production of the original writing cannot be obtained, resort may be had to secondary evidence.

Dunbar v. U. S., 156 U. S. 185;

Myrick v. U. S., 219 Fed. (1st);

Pilson v. U. S., 249 Fed. 328;

Maryland Casualty Co. v. Simmons, 2 Fed. (2d) 29; cert. denied 266 U. S. 634.

See, also:

Sprague, Tire & Rubber Co., 11 B. T. A. 610.

(C) Error in Rejecting the Secondary Evidence of Mark J. Sandrich, Certified Public Accountant.

THE FACTS.

After the presiding Judge had diverted the trend of the hearing as indicated in the discussion under the preceding point, he asked:

"Have you got anything more?"

The following colloquy then took place:

"Mr. Tonjes: I have nothing further, Your Honor, no, sir.

The Member: Have you got anything, Mr. Sandrich?

Mr. Sandrich: Nothing, Your Honor, except that I am making the offer to bring the rest of my records, my audit records of the Chiquita Mining Company, Limited, and offer them *in toto*.

The Member: You can't offer records that way, Mr. Sandrich. I think your difficulty, if I can be frank, is you are trying a law suit and you are a C. P. A. Now, there are ways to do these things. Cases are tried here in the same way as in the Federal District Court. They are governed by the rules of evidence. You can't just bring in a lot of documents and put them on the table.

Mr. Sandrich: Your Honor—

The Member: No, I have been pretty patient about this matter, and it seems to me that the time has come to conclude it, because I don't see where you have at all the evidence that is going to help you on the second point.

Mr. Sandrich: These documents that we speak of, Your Honor, my files, my working papers covering

that particular period of time do constitute the only existing record of those transactions.

Mr. Tonjes: Well, let the record show that I object to the offer as made, Your Honor.

Mr. Steffes: May I cite a precedent established—

The Member: No, I am going to hear Mr. Sandrich, not you.

Mr. Sandrich: Your Honor, isn't it a fact that a C. P. A. having made a detailed audit of a concern, that his evidence and his findings are competent in evidence as to sum totals and a general exposition of the events.

Mr. Tonjes: We have no such problem before the Board. We have no accounting problem involved here.

Mr. Sandrich: We have a question of fact involved, questions which I myself, as the auditor, as a certified public accountant, went into and verified and built up my records therefrom, and it seems to me that those would be competent evidence.

The Member: If I understand your second point, I will explain it to you, as to what I think is the point. Now, the Government has said that you must take the same basis for depletion that the previous owners of these mining claims had.

Mr. Sandrich: When you use the second person, Your Honor, do you mean Chiquita Mining Company, Limited, or any corporation or any mining company?

The Member: I mean specifically this company. Now, the law provides that where properties are transferred to a corporation for stock, and the same control and interest prevails, that then the corporation for depletion and depreciation takes the same basis as the transferor.

Mr. Sandrich: That is correct.

The Member: Now, if you do not fall within that provision, then, of course, where stock is issued the mining company, the successor company would take a basis equal to the fair market value of the property when they got it for the stock, or, in other words, the value of the stock, for the claims. Now, it seems to me the only way this point would have been proven would be to start out with your mining claims.

Mr. Sandrich: That is what I had intended to do, Your Honor.

The Member: All right. Show who owned them, show the relative interests of the several people in them, produce the contract whereby these claims were to be transferred to the mining company, produce your stock books and show what stock was issued, show the minutes giving the details of the transaction, and what not, and if that did not bring you within this restricted position, then you would prove your values here as a basis for depreciation, which would have to be a new basis, then, either based on the value of the claims or the cost of the stock, and the only way you could do that is to produce witnesses who know the value as of that time, the fair market value. You can't prove that by an audit you made.

Mr. Sandrich: No, Your Honor, but I can prove by an audit I made the way, the manner in which and the times at which certain quantities of capital stock, as a matter of fact, all of the capital stock, were issued, and my working papers happen to be the first adequate record prepared on those, from my working papers where the entries were copied into the stock ledger and journal. Now, as to valuation,

Mr. Maxfield and Mr. Wilton had a very intimate knowledge of that and were parties to the transactions.

The Member: There are plenty of people. I want to know what a building was worth here in Los Angeles ten years ago. It may be that there are people who handled the deal that know, but I may go out and get a real estate man who is an authority. He can testify.

Mr. Sandrich: Well, that—

The Member: I don't care to argue indefinitely with you.

Mr. Sandrich: In that case, Your Honor, wouldn't a letter from the Revenue Department in which, after examination, they had decided that those claims were worth a certain amount of money, be admissible?

Mr. Tonjes: No.

The Member: It is not admissible in this tribunal. You might get Government counsel to agree with you. That is a different thing. But it has no probative weight otherwise.

Well, we will close the record and I will allow the parties thirty days to file a memorandum in support of their position." [Tr. of Rec., pp. 103-106.]

It was at this point that the hearing was concluded.

The following three remarks made by Mr. Sandrich, the certified public accountant, show the offer made by him to testify concerning the precise question in dispute:

"Your Honor, isn't it a fact that a C. P. A. having made a detailed audit of a concern, that his evidence and his findings are competent in evidence as to sum totals and a general exposition of the events?"

"We have a question of fact involved, questions which I myself, as the auditor, as a certified public accountant, went into and verified and built up my records therefrom, and it seems to me that those would be competent evidence."

"No, Your Honor, but I can prove by an audit I made the way, the manner in which and the times at which certain quantities of capital stock, as a matter of fact, all of the capital stock, were issued, and my working papers happen to be the first adequate record prepared on those, from my working papers where the entries were copied into the stock ledger and journal. Now, as to valuation, Mr. Maxfield and Mr. Wilton had a very intimate knowledge of that and were parties to the transactions." [Tr. of Rec., pp. 104-106.]

ARGUMENT.

When we consider that one of the principal questions to be answered was the number of shares of its capital stock that petitioner had issued for the mining properties in question, the parties to whom said stock had been issued and the proportion of the stock thus representing the cost price of the mining properties to petitioner, to the total number of outstanding shares of the capital stock of petitioner at the time of the transaction in question, then it becomes self-evident that this proffered testimony on the part of the certified public accountant who had made a complete audit of all the book, records and affairs of the corporation from the time of its organization, was competent to prove the result of that audit with reference to the specific details under consideration.

Certainly he was a competent witness to testify concerning what his audit had disclosed with reference to the number of shares of the capital stock of petitioner that Jack H. Smith and Otto F. Schwartz had received as their share of the cost price paid by petitioner for the mining properties conveyed to it by them. The witness was also competent to testify concerning the number of shares of the capital stock of petitioner that the Chiquita Mine Syndicate had received. The witness was eminently qualified to testify concerning what proportion of the outstanding capital stock of petitioner the said Jack H. Smith and Otto F. Schwartz owned at any time after the organization of the corporation, and particularly at the time of, and after, the conveyance by them of the mining properties to petitioner. The witness was best qualified to give his expert testimony concerning what his audit had disclosed with reference to the stock control of the corporation from the time shares of stock were first issued by petitioner.

Instead of rejecting this evidence, it would seem that both counsel for respondent and the Court should have welcomed it.

As Mr. Sandrich himself suggested to the Court, the present situation is clearly one which falls within the rule that a qualified auditor and certified public accountant can testify concerning the totals of numerous items which he has obtained after a careful and complete examination and audit of the records reflecting such items. We believe that this contention on our part is so reasonable and unanswerable that we shall not argue the point further.

AUTHORITIES.

The testimony of the certified public accountant who made a complete examination of the books and records of petitioner, with reference to the results of said examination and audit, was competent evidence.

Brown v. U. S., 142 Fed. 1;
Galbreath v. U. S., 257 Fed. 648;
Cooper v. U. S., 9 Fed. (2d) 216;
Arine v. U. S., 10 Fed. (2d) 778.

(D) Error in Rejecting the Books and Records of Petitioner in the Possession of Mark J. Sandrich, Certified Public Accountant.

THE FACTS.

We have already quoted that portion of the record wherein Mark J. Sandrich, the certified public accountant, offered to testify concerning the result of his examination and audit with reference to pertinent and relevant matters disclosed by the books of the corporation. Mr. Sandrich expressly made the offer to bring the entire audit records of petitioner into court and to introduce them *in toto*. This offer was refused. Previously in the examination of the attorney for petitioner, the following foundation was laid for the introduction of the records which had been prepared by the certified public account for petitioner:

> "Q. (By Mr. Sandrich) At any time during your representation of the company were you charged with the duty of retaining the services of a certified public accountant? A. (By Mr. Steffes) I was.
>
> Q. And for what purpose, please? A. We had certain litigation pending in the 8th Judicial District Court of the State of Nevada, in and for the County of Clark, on a mandamus proceeding, brought by a

stockholder or a small group of stockholders, and at that time I stated to the court that a complete audit would be made by a certified public accountant of all of the books and records of the corporation from the time the corporation first formed and took over the properties, up until the—up until that time or at the end of the taxable year, which was, I believe, December 31, 1938.

Q. Did you obtain the services of such an accountant? A. I did.

Q. And who was he, please? A. Mark J. Sandrich, a certified public accountant, in Los Angeles, California.

Q. Did you instruct the certified public accountant with regard to what you wanted him to do? A. I did.

Q. Will you kindly repeat the instructions that you gave him?

Mr. Tonjes: May I ask the purpose of this line of questioning, Your Honor? I think it would be pertinent.

Mr. Sandrich: Yes, Your Honor. I have explained before that the company had no books and records. What I am leading up to is an offer of my audit records of that period as the records of the corporation.

The Member: Well, as I understand the question, on the point that is being tried, of the rate of depreciation on certain mining machinery and equipment, the parties are in agreement on the cost: the question is, what is the life? I can't see where a lot of this testimony is relevant.

Mr. Sandrich: There seems to have been some difference of opinion, Your Honor, or at least difficulty regarding amounts and dates and quantities,

and I wanted my records here for the benefit of counsel for respondent and myself.

The Member: Well, it seems to me it would be very doubtful whether it is admissible, but I would have to reserve that until it is offered and see just exactly how it is offered." [Tr. of Rec., pp. 71-73.]

ARGUMENT.

The records which Mr. Sandrich desired and attempted to introduce into evidence were actually the then permanent records of petitioner relating to the early affairs of petitioner, particularly at the time of the transaction wherein and whereby petitioner acquired the mining properties which produced the income on which the tax was levied. As he stated, at first the corporation had no formal set of books; but after he made his audit, this audit spread was retained as part of the permanent records of the corporation, for all transactions which had occurred prior to Mr. Sandrich having set up a more formal and elaborate set of books and records.

Had he been permitted to testify, then counsel for respondent could easily have verified every single item concerning which he testified from the records that he offered to produce in court. From these records the witness could have traced each item to its original source, and could have identified the shares of stock that had been issued as the cost price of the mining properties acquired by petitioner.

This assignment of error relative to the rejection of the books and records of petitioner, as evidence, as well as the rejection of the testimony of Mr. Sandrich, discussed under the preceding point, is predicated on the premise that counsel for respondent had waived all objection to secondary evidence. In making this statement,

we are not receding from our position, however, that the books and records offered by Mr. Sandrich were in fact primary evidence.

It is difficult for us to understand how these books and records could properly be excluded. The only possible theory for excluding them would be that the proof should be restricted to certain written agreements which petitioner was unable to produce at the hearing. That theory, however, is neither proper, legal, just, nor equitable. It demonstrates also what we have contended before—that the rulings of the Court considered as a whole clearly showed that the proof in this case was unduly restricted to those written instruments, and that in thus restricting the proof, the learned trial Judge erred.

AUTHORITIES.

The modern rule is that practically any regular entry or record properly verified, including a subsidiary slip, memorandum or note, is admissible.

Robilio v. U. S., 291 Fed. 975; Cert. Denied, 263 U. S. 716;

E. I. Du Pont de Nemours & Co. v. Tomlinson, 296 Fed. 634;

Massachusetts Bonding & Ins. Co. v. Norwich Pharmacal Co., 18 Fed. (2d) 934;

Cub Fork Coal Co. v. Fairmont Glass Co., 19 Fed. (2d) 273.

In 1936, Congress, acting upon the recommendation of the Attorney General, passed an act adopting the liberal rule for the introduction of records, for all federal courts.

28 U. S. C. A. (June 20, 1936), c. 640, Sec. 9, 49 Stat. L. 1564.

IV.

The Court Erred in Rejecting Evidence on the Question as to Whether the Commissioner Was Estopped to Deny the Cost to Petitioner of Said Mining Claims to Be $500,000.00, by Reason of Two Previous Determinations to That Effect by the Internal Revenue Department.

The Facts.

We have already shown the manner in which the Internal Revenue Department on two previous occasions determined the consideration that had been paid by petitioner as the cost price of the mining properties which it acquired.

Argument.

As we argued above, when the Internal Revenue Department made its previous inquiries and determinations, it was then making a direct determination on each occasion with reference to the consideration paid by petitioner for said mining property.

In the present inquiry, which involves a permissible deduction in the ascertainment of the amount of income received by petitioner upon which it was obligated to pay an income tax, such determination of the cost price to petitioner of the mining properties is more indirect.

Certainly, if petitioner had adopted the government's theories on these previous occasions (which in fact it did), it would not be in a favorable position if it now attempted

to repudiate such position upon which its former tax, on two occasions, was based.

Had these previous matters been determined after a court hearing, and had the determinations been made by the Court instead of by the Internal Revenue Department, the matter would have become *res adjudicata,* and there would have arisen against respondent an estoppel by judgment. In the absence of such judgment, there should, however, be an estoppel *in pais.*

The doctrine of estoppel has thus been expressed:

> "Whoever has by any declaration, act or omission deliberately and intentionally led another to believe a certain thing to be true, and to act upon such belief, in any litigation arising out of such declaration, act or omission, he shall not be permitted to falsify it."

AUTHORITIES.

The doctrine of estoppel can be invoked in matters of tax liability.

> *Burnet v. San Joaquin Fruit & Invest. Co.,* 52 Fed. (2d) 123, 10 A. F. T. R. 399.

V.

The Court Erred in Denying Petitioner's Motion to Reopen This Cause for the Presentation of Further Evidence Upon the Issue of the Allowance of a Proper Rate for Depletion of the Ores in the Properties Owned by the Petitioner.

The Facts.

After the trial Judge in his memorandum opinion had held that respondent's determination on the issue of depletion should be approved for the reason that no evidence was offered on that issue, petitioner moved the Court to reopen the cause for the presentation of further evidence upon the issue of the allowance of a proper rate for depletion of the ores in the properties owned by petitioner.

This motion was supported by three affidavits, which are set forth at length on pages 28 to 32 of the transcript of record. The affidavits clearly showed a sufficient justification or excuse for not having produced the documentary evidence to which the trial judge had obviously restricted the proof.

Argument.

The question presented under this point involves a determination as to whether the trial judge properly exercised the discretion that was vested in him.

Counsel for petitioner had explained the absence of the written agreements in that they had previously been delivered to the Treasury Department and to the S. E. C., and that counsel for petitioner had been unable to get hold of them. [Tr. of Rec., p. 80.]

In view of the fact that the trial judge so strongly insisted that the question of the vendors' control of the affairs of petitioner after the mining properties had been conveyed to petitioner be proved exclusively by these written contracts, a reasonable opportunity should have been accorded petitioner to produce the desired evidence.

We sincerely feel that since the Court did not permit the introduction of secondary evidence even after counsel for respondent had consented thereto, as we pointed out above, it abused its discretion in not granting this motion of petitioner to reopen the cause for the purpose of obtaining and introducing the written contracts in question.

The collection of income taxes, though important, does not necessitate such quick action as would deprive a taxpayer of his day in court. This should be particularly true since petitioner had voluntarily paid an additional income tax of $7,000.00 after Mr. Sandrich was retained to make a complete audit of the affairs of the corporation and to do whatever was necessary to be done to disclose any additional tax liability. [Tr. of Rec., p. 70.]

Authorities.

In the case of *Chatham Phenix Natl. Bk. & Tr. Co. v. Helvering*, 87 Fed. (2d) 547, 18 A. F. T. R. 775, it was held that where it appeared that the petitioner had been represented before the Board of Tax Appeals by a person so unfamiliar with the Board's procedure and the facts of the case that the issue was not made clear, and there were

present other unusual and unfortunate circumstances, the Board should have reopened the case in the promotion of justice.

See, also:

Washburn Wire Co. v. Commissioner, 67 Fed. (2d) 658;

Helvering v. Continental Oil Co., 68 Fed. (2d) 750; Cert. Denied, 292 U. S. 627.

Conclusion.

From what has been said above, we believe that it has been sufficiently demonstrated that petitioner could have proved by competent evidence that the vendors, Jack H. Smith and Otto F. Schwartz, were not in as much control of the affairs of petitioner after petitioner had acquired the mining properties in question as they were prior thereto. Furthermore, if it was proper to restrict the proof to the written contracts, which had already been fully executed by all parties, then a reasonable opportunity should have been afforded petitioner to obtain and introduce these contracts.

Under all the circumstances of the case, we feel that it would be just and equitable to permit a further hearing on the issue of depletion, and that the trial judge's determination on that issue should be reversed for the purpose of having a full hearing thereon.

Respectfully submitted,

A. P. G. Steffes,

Attorney for Petitioner.